



PUBLIC UTILITIES COMMISSION

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June 30, 2022

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Ratesetting

TO PARTIES OF RECORD IN APPLICATION 20-04-017:

This is the proposed decision of Administrative Law Judge Watts-Zagha. Until and unless the Commission hears the item and votes to approve it, the proposed decision has no legal effect. This item may be heard, at the earliest, at the Commission's August 4, 2022 Business Meeting. To confirm when the item will be heard, please see the Business Meeting agenda, which is posted on the Commission's website 10 days before each Business Meeting.

Parties of record may file comments on the proposed decision as provided in Rule 14.3 of the Commission's Rules of Practice and Procedure.

The Commission may hold a Ratesetting Deliberative Meeting to consider this item in closed session in advance of the Business Meeting at which the item will be heard. In such event, notice of the Ratesetting Deliberative Meeting will appear in the Daily Calendar, which is posted on the Commission's website. If a Ratesetting Deliberative Meeting is scheduled, *ex parte* communications are prohibited pursuant to Rule 8.2(c)(4).

/s/ ANNE E. SIMON

Anne E. Simon

Chief Administrative Law Judge

AES:mph

Attachment

Decision **PROPOSED DECISION OF ALJ WATTS-ZAGHA** (Mailed 6/30/2022)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Joint Application of California-
American Water Company (U210W)
and Warring Water Service, Inc.
(U331W) for an Order Authorizing
East Warring Water Service, Inc. to
Sell and California-American Water to
Purchase the Water Utility Assets of
Warring Water Service, Inc.

Application 20-04-017

**DECISION APPROVING THE SALE OF WARRING WATER SERVICE, INC.
TO CALIFORNIA-AMERICAN WATER COMPANY INC.**

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**DECISION APPROVING THE SALE OF WARRING WATER SERVICE, INC.
TO CALIFORNIA-AMERICAN WATER COMPANY INC**

Summary

This decision approves the proposed uncontested purchase of the water utility assets of Warring Water Service, Inc. (Warring) by California American Water Company, Inc. (Cal-Am) for a purchase price of \$4,600,000, and authorizes Cal-Am to use the same value for ratemaking purposes as the rate base of the acquired system.

This decision authorizes the transfer of asset ownership from Warring to Cal-Am and modifies Cal-Am's Certificate of Public Convenience and Necessity to incorporate the Warring service area immediately into Cal-Am's Ventura County District for operational purposes. Rate changes necessitated by this acquisition will not occur until the next Cal-Am General Rate Case (GRC), and accordingly this decision defers the allocation of new rate base to the next GRC as well.

This decision denies the request to create The Warring Acquisition Contingency Memorandum Account but grants the request to create The Warring Transaction Cost Memorandum Account, limited to any eligible costs incurred after the date of this decision. This decision authorizes the inclusion of the service territory acquired from Warring in Cal-Am's existing Memorandum Account for Environmental Improvements and Compliance issues for Acquisitions.

Finally, this decision grants Cal-Am's request for interim rate relief and closes the proceeding.

1. Background

1.1. Procedural Background

On April 27, 2020, the California American Water Company (Cal-Am) and Warring Water Service, Inc. (Warring), collectively, the Joint Applicants, filed Application (A.) 20-04-017. On May 28, 2020, the Public Advocates Office timely filed a protest. On July 14, 2020, a prehearing conference was conducted by the assigned Administrative Law Judge (ALJ).

On January 27, 2021, the assigned Commissioner issued a Scoping Memo and Ruling. On February 24, 2021, the Public Advocates Office at the California Public Utilities Commission (Cal Advocates) submitted the Motion to Withdraw as a Party (Motion to Withdraw). In the Motion to Withdraw, Cal Advocates states that upon review of the Joint Applicants' testimony, discovery responses, and the proceeding scope, from its perspective "there are no disputed issues within the scope of the proceeding."¹ On February 26, 2021, the Joint Applicants responded to the motion, with a recommendation that Joint Applicants' exhibits be introduced into evidence and the case submitted.

The assigned ALJ issued a ruling granting the motion for the Public Advocates Office to withdraw as a party on March 25, 2021 and provided procedural instruction to the Joint Applicants. The Joint Applicants filed their motion to admit exhibits into the evidentiary record on March 26, 2021 and the matter was submitted at that time. The proceeding was reassigned to ALJ Camille Watts-Zagha on June 15, 2021 and to Commissioner John Reynolds on February 15, 2022.

¹ Motion of the Public Advocates Office at the California Public Utilities Commission, dated February 24, 2021, at 2.

The record of this proceeding consists of all filed documents and testimony received into the evidentiary record.

1.2. Joint Applicants

The Joint Applicants are Warring and Cal-Am. Warring is a privately owned, Commission-regulated small water utility owned in equal parts by DeLores Pace and Gill Giddings. Warring's first of three wells was dug in the 1920's, and the system has been owned and operated by the Warring family since its incorporation in 1966. The current owners inherited their interest in the system from their husbands in 2002 and 2006. Warring serves 518 customers in and near the town of Piru, in Ventura, California. In addition, there are 343 planned residential units in the Warring service area. The Commission classifies a utility of Warring's size as Class D.

Cal-Am, a California corporation, is a subsidiary of American Water Works Company, which is the largest publicly traded water utility in the United States, serving approximately 16 million people in North America. As a Class A California water utility, Cal-Am serves a population of approximately 680,000 people in 50 communities, spread across approximately 10 districts. The Commission sets rates for each of these districts in regularly scheduled General Rate Cases (GRCs). In terms of customers served, Cal-Am increased six-fold over the last twenty years. Most recently, Cal-Am acquired Oxbow Mutual Water Company and Dunnigan Water Works in 2015, Adams Ranch,

Meadowbrook² and Geyserville Water Works in 2016, Rio Plaza,³ Hillview,⁴ Fruitridge Vista⁵ in 2019, and East Pasadena Water Company in 2021.⁶

Cal-Am's GRC application for 2021 was approved by the Commission in Decision (D.) .21-11-018 on November 15, 2021.⁷ Cal-Am anticipates filing its next GRC application in July 2022 for rates to become effective in 2024.

1.3. Application and Proposed Acquisition Terms

In the instant application, the Joint Applicants request Commission authority for Cal-Am to acquire the assets of Warring and assume the public utility operations of Warring, as described in the purchase agreement between Cal-Am and Warring (Proposed Acquisition), dated April 16, 2019 (Asset Purchase Agreement). Through this Proposed Acquisition, Cal-Am would acquire the Warring water distribution system which consists of three groundwater wells (two active and one emergency supplemental flow), one storage tank with a 1.1 million gallon capacity, distribution pipelines, fire hydrants, isolation valves, and air release valves. The Proposed Acquisition and the Asset Purchase Agreement also includes provisions to offer full-time employment to the Warring operations employee. Through this system, Warring

² D.16-12-014.

³ D.19-04-015.

⁴ D.19-04-015.

⁵ D.19-12-038.

⁶ D.21-08-002.

⁷ D.21-11-018 approving Cal-Am's 2021 General Rate Case (GRC) Application (A.)19-07-004 was issued November 18, 2021 and D.22-01-020 correcting errors in D.21-11-018 was issued January 14, 2022.

serves 518 customers, with an additional 343 residential service connections under development.⁸

Cal-Am also proposes to consolidate Warring into Cal-Am's Ventura County District for operational purposes, based on Warring's physical proximity (Warring is 32 miles from the area served by Cal-Am) to the Cal-Am Ventura County District operational facility. The operational consolidation would occur immediately once the acquisition closes.

With regard to ratemaking, Cal-Am proposes leaving the current Warring rates in effect, including approval to continue to file for standard rate increases indexed to inflation, until the next Cal-Am GRC is approved, anticipated to be 2024. Then Warring would cease to exist as a separate water utility. Its former customers would be served by Cal-Am under Cal-Am's Certificate of Public Convenience and Necessity (CPCN) and Cal-Am's CPCN would be modified by this decision to encompass the area formerly served by Warring.

At the time Joint Applicants filed this application in April 2020, Cal-Am proposed consolidating Warring into Cal-Am's Los Angeles County District for ratemaking purposes, on the rationale that Warring and Los Angeles County District cost structures are similar in nature as their main water sources are groundwater.⁹ Since that time, the Commission approved Cal-Am's request to consolidate, for ratemaking purposes, its Los Angeles, Ventura and San Diego County Districts into one Southern Division.¹⁰ This decision thus refers to the

⁸ Application at 4.

⁹ CAW-2 (Owens) at 8-9.

¹⁰ D.21-11-018 approved three settlements, resolved the remaining disputed issues raised by the Cal-Am General Rate Case Application (A.) 19-07-004, and authorized rate increases in the years 2021 through 2023.

Southern Division where the Joint Applicants may have referred to the Los Angeles County District.

The Joint Applicants contend that the \$4.6 million purchase price, with possible adjustments at the time the sale closes, represents the fair market value of the Warring assets and seeks Commission approval of that value.¹¹ These assets currently have a book value of approximately \$745,867. Capital invested for the new developments brings Warring's rate base for ratesetting purposes to approximately \$1.384 million. Warring's approved revenue requirement of \$500,800 was established by Commission Resolution W-4796 in 2009 and is forecast to be \$644,100 in 2021. As discussed below, current law allows Cal-Am to include the fair market value of the assets in its rate base for ratesetting purposes. Thus, as proposed, this transaction would add \$3.2 million to the combined rate base of Cal-Am. The difference between the rate base valuation before and after acquisition is known as the "acquisition premium." As an increase to rate base also requires an increase in revenue and rates to produce Cal-Am's authorized rate of return, the overall revenue increase to all Cal-Am customers, including the customers of the former Warring, would have amounted to an estimated 0.35 percent.

However, when including the additional revenues already generated by Warring currently, the revenue and rate impact of this acquisition to all Cal-Am customers will amount to an estimated 0.12 percent, or less than 15 cents per average customer bill, depending on the ratemaking district.

¹¹ Exhibit 3 to CAW-1C (Hofer Confidential) itemizes the Adjustments to the Purchase Price to be made as of closing.

2. Issues Before the Commission

The issues before the Commission are:

- A. Whether the Proposed Acquisition will serve the public interest and should be approved and, if so, whether it should be approved with conditions;
- B. What is the fair market value of the purchased assets;
- C. Whether the proposed purchase price is reasonable;
- E. Whether the entire proposed purchase price should be included in Cal-Am's rate base;
- F. Whether the Proposed Acquisition would result in benefits to both Warring and Cal-Am ratepayers;
- G. Whether Cal-Am's customers have been properly noticed in accordance with the requirements of Commission Rule 3.2;
- H. Whether the Commission should approve Cal-Am's proposals for operational and ratemaking consolidation of the Warring service area with Cal-Am's existing service areas?
- I. Whether the Commission should authorize the ratesetting and cost tracking proposals in the Application, including creation/expansion of memorandum accounts and the costs to be tracked therein, as well as interim rates and rate base increases prior to consolidation?
- J. Whether Cal-Am is financially and operationally qualified to acquire Warring's water system and should be granted an expansion of its existing CPCN to include Warring's service territory?
- K. Whether the Commission should relieve Warring of its CPCN following the conclusion of the Proposed Acquisition?

3. Admittance of Testimony and Exhibits into Record

Evidentiary hearings were not held as the application became unopposed upon the withdrawal of the Public Advocates Office as a party. The

Commission's Rule 13.8 permits prepared testimony to be offered into evidence as an exhibit in lieu of oral testimony under direct examination. The Joint Applicants filed their motion to admit the below identified exhibits into the evidentiary record (Motion) on March 26, 2021. The Motion is unopposed and is granted. Accordingly, the Joint Applicants' proposed exhibits are marked, identified and received into evidence as listed below.

Exhibit Number	Sponsor/Witness	Description
CAW-1	Cal-Am/Hofer	Direct Testimony of Garry M. Hofer, Public Version, dated April 27, 2020
CAW-1C	Cal-Am/Hofer	Direct Testimony of Garry M. Hofer, Confidential Version, dated April 27, 2020
CAW-2	Cal-Am/Owens	Direct Testimony of Stephen Wesley Owens, dated April 27, 2020
CAW-3	Cal-Am/Wademan	Direct Testimony of Michael Wademan, dated April 27, 2020
WWS-1	WWS/Brommenschenkel	Direct Testimony of Frank Brommenschenkel dated April 27, 2020
WWS-2	WWS/Pace	Direct Testimony of Glen Pace, dated April 27, 2020
JA-1	JA/Zanni	Direct Testimony of Kevin M. Zanni, dated April 27, 2020

4. Applicable Legal Framework

As we review the Joint Applicant's Proposed Acquisition,¹² the Commission must find the proposed sale and asset purchase transaction to be in the public interest according to Pub. Util. Code §§ 851 *et seq.*, as illuminated by

¹² The Joint Applicants have complied with the procedural requirements of §§ 851–854 and §§ 2718–2720, and filed the requisite supporting documents identified in Rule 3.6 of the Commission's Rules of Practice and Procedure and in Decision (D.) 99-10-064.

§§ 2718 *et seq.* We will also address §§ 451 *et seq.*, as applied to the Proposed Acquisition.

4.1. Sections 851 *et seq.*

Section 851, in relevant part, requires Commission approval before a public utility may sell the whole or any part of its property or rights “necessary or useful in the performance of its duties to the public,” and § 854(a) requires Commission authorization before any person or corporation may acquire or merge with any public utility. The Commission has long interpreted these code sections to prohibit acquisitions, mergers, and transfers of control unless the Commission has found the proposed transaction to be in the public interest.¹³

In addition, subsections (b), (c), and (d) of § 854 contain a list of public interest criteria for transactions involving electric, gas and telephone corporations.¹⁴ Although these subsections, by their terms, do not apply to water utilities, the Commission has referred to these public interest criteria in its review of proposed water utility transactions to identify various aspects of the public interest.¹⁵

Here, we reference the eight criteria in subsection (c) primarily to emphasize that the public interest is comprised of a mix of interests: ratepayer interests, shareholder interests, public utility employee interests, as well as local and statewide community interests.¹⁶

¹³ See, Decision (D.) 99-10-064 at 5-6; D.01-09-057 at 23-29; D.10-09-012 at 6, 8; D.11-12-007 at 5-8; D.15-12-029 at 11; D.16-12-014 at 12; D.19-04-015 at 6; D.19-12-038 at 7.

¹⁴ Section 854 subsection (d) applies only to electric and gas corporations.

¹⁵ D.01-09-057, Conclusions of Law 8, 9.

¹⁶ Subsection (c) of § 854 contains a list of eight public interest criteria, as follows:

Subsection (e) of § 854 also applies here and provides, as follows:

When reviewing a merger, acquisition, or control proposal, the commission shall consider reasonable options to the proposal recommended by other parties, including no new merger, acquisition, or control, to determine whether comparable short-term and long-term economic savings can be achieved through other means while avoiding the possible adverse consequences of the proposal.

4.2. Sections 2718 -2720

The Public Water System Investment and Consolidation Act of 1997 was codified in §§ 2718 -2720 and declares:

- a) Public water systems are faced with the need to replace or upgrade the public water system infrastructure to meet increasingly stringent state and federal safe drinking water laws and regulations governing fire flow standards for public fire protection.
- b) Increasing amounts of capital are required to finance the necessary investment in public water system infrastructure.

-
- (1) Maintain or improve the financial condition of the resulting public utility doing business in the state.
 - (2) Maintain or improve the quality of service to public utility ratepayers in the state.
 - (3) Maintain or improve the quality of management of the resulting public utility doing business in the state.
 - (4) Be fair and reasonable to affected public utility employees, including both union and nonunion employees.
 - (5) Be fair and reasonable to the majority of all affected public utility shareholders.
 - (6) Be beneficial on an overall basis to state and local economies, and to the communities in the area served by the resulting public utility.
 - (7) Preserve the jurisdiction of the commission and the capacity of the commission to effectively regulate and audit public utility operations in the state.
 - (8) Provide mitigation measures to prevent significant adverse consequences that may result.

- c) Scale economies are achievable in the operation of public water systems.
- d) Providing water corporations with an incentive to achieve these scale economies will provide benefits to ratepayers.¹⁷

The Consolidation Act sets out a framework to incentivize acquisitions of small water systems by larger, more financially secure entities, while leaving intact the Commission existing “powers and responsibilities granted pursuant to Sections 851 and 852.”¹⁸ Significantly, § 2720, subsection (a) provides, “The commission shall use the standard of fair market value when establishing the rate base value for the distribution system of a public water system acquired by a water corporation.”

The Commission established guidelines for the implementation of the Consolidation Act in D. 99-10-064.¹⁹ Among other things, the guidelines distinguish the authority for applications governed by the Consolidation Act from § 851 applications for the sale of utility property.²⁰

The Consolidation Act requires the Commission to include in the acquiring water company’s rate base the fair market value of the acquired assets.²¹ The fair market value is determined in accordance with § 2720(a), as the purchase price (below appraisal) agreed to by a willing buyer and willing seller. When the fair market value exceeds the reproduction cost of the acquired system, the Commission shall further determine whether fair and reasonable to also include

¹⁷ § 2719.

¹⁸ § 2720(d).

¹⁹ D.99-10-064, Findings of Fact (FoF) 3, 4.

²⁰ D.99-10-064 at 5.

²¹ This transaction is governed by § 2720 (a). Subsection (b) to § 2720 becomes applicable when the fair market value exceeds reproduction cost, which is not the case here.

the excess in rate base in accordance with § 2720(b). The difference between the book value of the assets prior to acquisition, and fair market value approved for inclusion in rate base is known as an acquisition premium.

Recovering the acquisition premium in rates provides an incentive for the larger companies to acquire the small water systems, but it does not create a legal presumption that any acquisition of a smaller water system by a larger entity is in the public interest. Rather, by referring to § 851, the Legislature indicated that the acquisition must first be determined to be in the public interest. In our consideration of the public interest, we employ relevant guidance from D.99-10-064, specifically:

The standards set for approval of applications provide a method to assess whether the goals of SB 1268 [Public Water System Investment and Consolidation Act] are met, that is, whether a transaction achieves maximum economies of scale, provides quality system improvements or provides benefits to customers.²²

4.3. Public Interest Review and Ratepayer Indifference Standard

Prior to the enactment of the Consolidation Act, once the transaction was determined to be in the public interest according to § 851, the acquiring company's new rate base after the acquisition would have been the value that was on the acquired utility's books. Now, however, we must look to the public interest considerations in §§ 851 *et seq.*, as well as §§ 2718 *et seq.*

In weighing the public interest considerations, there have been a handful of Commission decisions applying the “tangible ratepayer benefit,”²³ standard

²² D.99-10-064 at 9.

²³ D.11-12-007 at 5-6 ultimately settled upon the “ratepayer indifference standard,” as did D.00-05-027 (*also see* Dissent), D.00-05-047 (*also see* Concurrence), D.10-09-012 at 8, D.15-12-029

which requires a finding that there is a tangible benefit to ratepayers. By and large, in similar water utility acquisition cases, the Commission has more routinely applied the “ratepayer indifference standard” which requires a finding that is no harm or adverse impact to the ratepayers.

In fact, the recent decision approving Cal-Am’s acquisition of East Pasadena Water Company is similar to this Proposed Acquisition as it consolidates an older, independent small Southern California water system with Cal-Am’s nearby districts to increase the system abilities to meet increasingly stringent water standards and realize economies of scale.²⁴

In reviewing this Proposed Acquisition, we are persuaded by those prior decisions and also compelled by the legislatively declared public interests, as set forth the Consolidation Act and discussed further in the following section of this decision, and determine the “ratepayer indifference standard” shall apply to our weighing of the public interest considerations.

4.4. Post-Transaction Ratemaking Under Section 2720 and Sections 451 et seq.

Subsection (a) of § 2720 established the post-acquisition ratemaking for this type of transaction:

The commission shall use the standard of fair market value when establishing the rate base value for the distribution system of a public water system acquired by a water corporation. This standard shall be used for ratesetting.

D.99-10-064 describes how adoption of the fair market value as the rate base value of the acquired system in accordance with Pub. Util. Code § 2720 was

at 11, D.16-12-014 at 12, D.15-11-012. In contrast, D.01-09-057 at 27, and D.19-12-038 at 7 apply the “net ratepayer benefits.”

²⁴ D.21-08-002.

uncontroversial, given § 2720.²⁵ In D.99-10-064, the Commission highlighted the “distinct power and obligation of the Commission to establish just and reasonable rates for services or commodities rendered by a public utility,” under § 451 *et seq.*²⁶ While water utility sales and acquisitions generally occur independent of GRCs, sales and acquisitions create new costs and savings, as does the statutory requirement in §2720 (a). Even once the acquisition is approved and operational consolidation occurs, the new costs and savings will take time to materialize.

Nevertheless, a Commission decision or resolution authorizing rates is a prerequisite to the implementation of rates for an acquired utility. Every water corporation is required to submit a GRC application every three years pursuant to § 455.2(c) and the Commission’s currently in effect rate case plan for Class A companies which includes Cal-Am. This two-step Commission approval process, first of the acquisition and secondly at the time the next GRC occurs, combined with the realization of costs and savings over time, suggests that rate impacts associated with the acquisition will differ in the short, medium and long-term.

Under the Consolidation Act, an acquisition premium for the Proposed Acquisition is permitted as long as the transaction is determined to be in the public interest, with reference to the guidance set forth in part of § 2720(b):

... whether the acquisition of the public water system will improve water system reliability, whether the ability of the water system to comply with health and safety regulations is improved, whether the water corporation by acquiring the public water system can achieve efficiencies and

²⁵ D.99-10-064 at 5, and at 9.

²⁶ D.99-10-064 at 10, Conclusion of Law 5, Ordering Paragraph (OP) 2.

economies of scale that would not otherwise be available, and whether the effect on existing customers of the water corporation and the acquired public water system is fair and reasonable.

Such premium will ultimately result in an increase in the utility's revenue requirement and corresponding increase in customer rates. While the Proposed Acquisition transaction occurs outside of the normal GRC proceeding, the Commission is mindful of the impacts on ratepayers when evaluating the public interest considerations associated with the Proposed Acquisition.

5. Discussion

The threshold issue is whether the Proposed Acquisition is in the public interest. As discussed below, we find that it is in the public interest and consistent with §§ 851 *et seq.*, §§ 2718 *et seq.*, and D.99-10-064.

5.1. The Proposed Transaction is in the Public Interest

Here, we apply the "ratepayer indifference standard" which requires a finding of no harm or adverse impact to the ratepayers, as discussed in section 4.3 of this decision. We weigh the public interest considerations and find that the Proposed Acquisition is in the public interest, as further discussed below.

Cal-Am argues that this Proposed Acquisition is in the public interest as the capital investment supports several desirable policy objectives, such as promoting safety, and putting Warring on stable financial footing to meet increasingly stringent state and federal safe drinking water laws and regulations relating to fire flow and protection.²⁷ Cal-Am further argues that economies of scale gained by folding Warring into Cal-Am's operations is achieved with little difference in cost to the ratepayers, and the promise of future cost savings over

²⁷ CAW-2 (Owens) at 2.

time beyond what is quantified in the application, from spreading fixed costs over a larger customer base, stating Cal-Am's "size, position in the industry and association with parent company American Water, will allow California American Water to meet water quality, reliability and customer service standards efficiently."²⁸

Cal-Am's witness Gary Hofer describes the Cal-Am safety programs that will extend to Warring customers upon the operational consolidation of the systems. He also describes the risk management measures that Cal-Am will employ to mitigate the risks posed by wildfires, as the Warring system is located in an extreme fire risk zone.²⁹ Stephen Owens, Cal-Am's Director of Rates, identifies an expectation that Warring "will require significant investment in the coming years," and provides evidence of Cal-Am's access to capital necessary to meet those needs.³⁰ Owens enumerates how larger water utilities achieve scale economies, including keeping expertise in-house, making the utility less dependent on costly outside consultants, and allowing the utility to benefit from the training and knowledge developed by in-house personnel. Owens asserts that the sizable workforce of a larger utility, with overlapping skills, makes absences less likely, improves response time to system and customer needs, and allows for more advanced equipment and technology.³¹

Owens also provides examples of lower costs per customer that will arise in the areas of 1) compliance with regulatory requirements, 2) maintaining customer information and billing systems, 3) purchasing

²⁸ CAW-2 (Owens) at 21-23.

²⁹ CAW-1 (Hofer) at 6-8.

³⁰ CAW-2 (Owens Direct) at 22-23.

³¹ CAW-2 (Owens) at 24.

materials and supplies, 4) maintaining high levels of customer service, 5) maintaining and improving quality of treated water, 6) providing for current infrastructure needs and future growth, and 7) supporting a level of expertise required to navigate often complex requirements for government programs such as grant funds and revolving fund loans.³²

Cal-Am also describes the customer programs that will be made available to Warring's former customers, including a more established water conservation program with offers to customers with high consumption service connections for audits, water saving equipment, and one-on-one attention. All customers would be afforded access to rebates for turf replacement, free water-saving devices. Cal-Am offers qualifying low-income customers bill discounts, with coordination in place to identify these customers and operate the assistance program with low per-customer costs and its low-income customers would have access to a low-income assistance program, a program that Warring lacks.

Warring's Regulatory and Operations Consultant Mr. Brommenschenkel describes Cal-Am as the logical company to acquire Warring, as Cal-Am operates other systems nearby, with a wide range of expert personnel to oversee the system, in contrast to Warring's sole system operator, and with the resources to spend on new water treatment expected to be required.³³ Mr. Brommenschenkel further describes the current owners as remotely involved, and the Warring system as one that "requires continual capital investment, leaving little financial benefit" for its aging owners.³⁴

³² CAW-2 (Owens) at 24-25.

³³ WWS-1 (Brommenschenkel) at 5.

³⁴ WWS-1 (Brommenschenkel) at 4.

Cal-Am contends that it has better access to capital at lower costs than Warring. Cal-Am's current cost of capital is 7.61 percent, lower than Warring's 13.75 percent.³⁵ Additionally, the Commission has previously authorized Cal-Am to issue up to \$359 million in long-term debt in D.18-07-013, and Cal-Am is also a part of a financial services agreement with its parent company that applies to all of its subsidiaries.³⁶ This suggests that Cal-Am is far more capable than Warring to finance future infrastructure needs. The resulting improvement in access to capital to invest in Warring's water system infrastructure is consistent with the policy objective of the Consolidation Act.

With regard to the effect on Cal-Am customers, they will benefit from the increased financial stability that comes from absorbing a nearby system with no identified deficits and with promising growth prospects,³⁷ bringing more customers from whom to recover the fixed costs of the system. Some of the synergies and cost savings have already been quantified and others are generally predicted, similar to the statutory expectation of § 2720. Cal-Am quantifies approximately \$175,000 in savings expected.³⁸ Cal-Am will utilize the addition of the new employee (currently employed by Warring) for additional operational flexibility in serving three formerly independent water districts: Cal-Am's Ventura County District, Warring, and customers of the former Rio Plaza Water

³⁵ Application at 8. Warring's rate of return of 13.75 percent was authorized in 2009 by Commission Resolution W-4796.

³⁶ CAW-2 (Owens) at 23.

³⁷ WWS-1 (Brommenschenkel) at 5-6.

³⁸ CAW-2 (Owens) at 12.

Company,³⁹ as attested to by Cal-Am's witness Hofer.⁴⁰ The quantified savings and Warring revenues cover more than a quarter of the revenues that would be required as a result \$3.2 million acquisition premium.

The quantifiable costs and savings of this Proposed Acquisition, and the associated rate base impacts, are as follows.

³⁹ The Commission approved Cal-Am's acquisition of Rio Plaza Water Company in D.18-04-015.

⁴⁰ CAW-1 (Hofer) at 3.

Revenue Impact Comparison⁴¹

(Estimated based on 2021 forecast, with illustrative assumption that synergies occur in 2021)

	Warring & Cal-Am, Separate	Warring & Cal-Am, Consolidated	Difference in \$	Difference in %
Operating Expenses w/o Taxes, Depreciation	\$ 169,925,100	\$ 169,750,800	\$ (174,300)	-0.10%
Total Expenses	\$ 220,744,600	\$ 220,737,200	\$ (7,400)	-0.003%
Total Revenue Required, Accounting for Synergies and New Revenue associated with Acquisition Premium	\$ 273,268,300	\$ 273,590,400	\$ 322,100	0.12%
Rate Base	\$ 691,303,000	\$ 694,518,600	\$ 3,215,600	0.47%
Portion of Additional Rate Base (aka Acquisition Premium) Supported by Synergies & Warring Revenues (No Associated Revenue/Rate Impact)			\$871,000	
Portion of Additional Rate Base (aka Acquisition Premium) Requiring Rate Increase Associated with \$322,100 Revenue Increase)			\$2,344,600	

We determine the Proposed Transaction meets the “ratepayer indifference standard,” in that the nominal rate increase expected in the mid-term, described in detail in section 5.3, is outweighed by anticipated lower costs of service in the long-term, itemized by Cal-Am witness Owens. Overall, the Proposed Acquisition demonstrates some benefit to Warring and Cal-Am customers, as well as to the broader public. The Proposed Acquisition will result in superior water system management and greater resources for capital investment to

⁴¹ Attachment 1 to CAW-2 (Owens) at 10-12.

further California's regulatory and policy goals of sustainable provision of safe, reliable and affordable water. We find this unopposed Proposed Acquisition to be in the public interest.

5.2. Purchase Price as the Fair Market Value

As discussed below, the total final purchase price of \$4.6 million represents the fair market value as defined by Pub. Util. Code § 2720. We therefore authorize the inclusion of the total final purchase price in rate base.

Here, we must establish the fair market value of the Proposed Acquisition because that value would be used as the rate base for subsequent ratesetting proceedings. The Consolidation Act defines the fair market value of the water system as a transaction between a "willing seller-willing buyer" consistent with California Code of Civil Procedure Section 1263.320.⁴²

Joint Applicants argue that Warring willingly entered into the contract with Cal-Am and the sellers were under no pressure or obligation to agree to the sale.⁴³ The Warring testimony states the sellers "had in mind a minimum value necessary to compensate them for the inconveniences [sic] of ownership of the Warring system over the years and they held that position all through the negotiations."⁴⁴ Cal-Am and Warring asserted that they arrived at the agreed upon contract purchase price of \$4.6 million after arm's length bargaining.

⁴² Subsection (a)(2) of § 2720 adopts the same meaning of "fair market value" set forth in Section 1263.320 of the Code of Civil Procedure, which in turn sets forth two options for determining fair market value – (a) the highest price on the date of valuation that would be agreed to by a seller, being willing to sell... and a buyer, being ready, willing and able to buy...with full knowledge of all the uses and purposes for which the property is reasonably adaptable and available, and (b) [for property taken for which there is no relevant, comparable market] the value on the date of valuation as determined by any method of valuation that is just and equitable.

⁴³ WWS-1 (Brommenschenkel) at 4, CAW-2 (Owens) at 32-33.

⁴⁴ WWS-1 (Brommenschenkel) at 4.

In this case, the appraised value meets the statutory check that the fair market value not exceed the appraised value using the replacement cost new less depreciation method. The appraisal valued the Warring system assets at \$5.3 million, consisting of tangible property assets valued at \$4.4 million and real estate valued at \$973,000.⁴⁵ The evidence supports the conclusion that purchase price is the fair market value as established by subsection (a)(2) of § 2720.

We recognize that transactions authorized under the Consolidation Act, like this one, may lead to rate increases but will also likely lead to other important ratepayer benefits envisioned by the Consolidation Act. As stated in D.01-09-057, “[a]pplying Section 2720 places a cost on ratepayers: that of supporting a rate base higher than it would otherwise be because it is set at fair market value.”⁴⁶ That is by design to incentivize these transactions to “achieve these scale economies will provide benefits to ratepayers”⁴⁷ as well as other legislatively imputed public interests, set forth in statute.

Based upon the evidence and the controlling authorities, we are persuaded that the purchase price is the fair market value. We therefore find the final purchase price of \$4.6 million represents the fair market value as defined by Pub. Util. Code § 2720 -- a transaction between a “willing seller-willing buyer” consistent with California Code of Civil Procedure Section 1263.320.⁴⁸ We

⁴⁵ Attachment 2 at 5, to CAW-4 (Zanni).

⁴⁶ D.01-09-057 at 28.

⁴⁷ § 2719 (d).

⁴⁸ Section 1263.320 of the Code of Civil Procedure sets forth two options for determining fair market value – (a) the highest price on the date of valuation that would be agreed to by a seller, being willing to sell... and a buyer, being ready, willing and able to buy...with full knowledge of all the uses and purposes for which the property is reasonably adaptable and available, and (b) [for property taken for which there is no relevant, comparable market] the value on the date of valuation as determined by any method of valuation that is just and equitable.

therefore authorize rate base equal to the total final purchase price of \$4.6 million as the fair market value of the Warring Water's used and useful utility assets. The incentive that results from using the purchase price as the new rate base, was estimated by Cal-Am to require \$322,100 more in revenue requirement annually.⁴⁹

5.3. Rate Impacts of the Purchase Price in Rate Base

As discussed above, our finding of purchase price as the fair market value for the Proposed Acquisition includes an incentive, termed an "acquisition premium," to Cal-Am. The Consolidation Act provides that an acquisition premium shall be included in the acquiring water company's rate base. This premium refers to the difference between the book value of the assets prior to acquisition, and the actual price at which the assets are purchased. In reviewing the potential ratepayer impacts of the Proposed Acquisition and the acquisition premium, we find that there are sufficient benefits flowing from the transaction to offset any resultant rate increase, as discussed below.

Here, Cal-Am will realize an acquisition premium of \$3.2 million, the difference between the purchase price of \$4.6 million and the current Warring assets worth \$1.3 million.⁵⁰ Put another way, the post-transaction rate base will be \$3.2 million greater than the existing rate base for Warring. The cost savings and synergies from economies of scope and scale offset the new revenue that would have been required from the entire acquisition premium, leaving only \$2.3

⁴⁹ Attachment 1, figure in column/row labeled, respectively "Revenue Requirement of Rate Base Transferred to Corporate," and "Operating Revenues/Total Revenue," CAW-2 (Owens).

⁵⁰ \$1.384 million is Cal-Am's forecast of rate base of Warring in 2021 for ratemaking purposes. Acquisition premium=difference between fair market value and book value of Warring assets=\$4.6 million-\$1.384 million= \$3.215 million.

million of new rate base with which new revenue will be associated.⁵¹ The Joint Applicants estimate the corresponding revenue requirement increase of the \$2.3 million would be \$322,100 and claim that this \$322,100 in new revenue requirement would result in a 0.12 percent increase per bill for each customer of Cal-Am (including both existing customers and customers from the newly acquired Warring system.)

The Commission last reviewed Warring's revenue requirement and associated rates to meet its revenue requirement in a GRC proceeding in 2009⁵² which adopted \$745,867 as Warring's rate base on which investors have the opportunity to earn a 13.75 percent return, and the adopted overall revenue requirement was \$102,582.⁵³

The Commission's Water Division has authorized rate increases annually pursuant to Resolution W-4796. Accordingly, Warring customer rates increased 2.7 percent in 2010,⁵⁴ 1.5 percent in 2011,⁵⁵ with eight more changes between 2012 and 2018.⁵⁶ The most recent rate increase approved was 1.4 percent in June 2021.⁵⁷

Warring's residential customers average monthly bill in April 2020 was \$56, consisting of a fixed meter charge and a quantity rate for each unit of

⁵¹ See Attachment 1 to CAW-2 (Owens).

⁵² The Commission last approved Warring's revenues and rates in Commission Resolution W-4796 (Resolution W-4796).

⁵³ Resolution W-4796.

⁵⁴ AL 45W.

⁵⁵ AL 46W.

⁵⁶ AL 64W.

⁵⁷ AL 70W.

water.⁵⁸ As regulatory and environmental oversight expands, the need for specialized labor and equipment expands along with the associated fixed costs.⁵⁹ Unlike the large utilities, smaller utilities may find expanding fixed costs problematic because the customer base across which they spread those costs is small and often not “scalable.”⁶⁰

With the acquisition of smaller water utilities, economies of scale allow for greater cost spreading, driving down per-customer costs of service.⁶¹ While both Warring and Cal-Am customers will see a 0.12 percent increase in their monthly bills after the acquisition, in testimony, Cal-Am provides that the acquisition will provide a benefit to both Warring and current Cal-Am Ventura County District customers, most notably the economies of scale benefits.⁶² Cal-Am quantified some of these savings from economies of scale in its projections for 2021.⁶³ The Joint Applicants asserted, and we agree, such economies of scale for Warring customers could grow over time. Additionally, in the short-term, Warring customers will gain access to a number of Cal-Am programs and services not offered by Warring, including:

- Nearby locations for expanded customer service and more effective assistance in emergency situations;⁶⁴

⁵⁸ Attachment 2 to CAW-2 (Owens).

⁵⁹ CAW-2 (Owens) at 24.

⁶⁰ CAW-2 (Owens) at 24.

⁶¹ CAW-2 (Owens) at 24.

⁶² CAW-1 (Hofer) at 5.

⁶³ Attachment 1 to CAW-2 (Owens).

⁶⁴ CAW-2 (Owens) at 29.

- Self-service options over the internet, paperless billing, translation in several languages;⁶⁵
- Low-income assistance for qualifying customers;⁶⁶ and
- More robust conservation programs.⁶⁷

Cal-Am expects the long-term synergies from the Proposed Acquisition to offset any rate increases to customers of the former Warring, stating:

While initial increases to the revenue requirement under California American Water appear to be slightly higher than they would if Warring continued to operate the system, Warring customers should experience the benefits of lower overall costs going forward.⁶⁸

We find that the short and long term benefits of this Proposed Acquisition for Warring customers, Cal-Am's existing customers in its Southern Division and all of Cal-Am's customers statewide sufficiently outweigh the anticipated rate increase. The Joint Applicants have adequately established that benefits will likely occur for all customers affected by the Proposed Acquisition, sufficient to justify an overall revenue increase estimated at \$322,100 annually. Moreover, the rates for Warring customers or for existing Cal-Am customers will not change

⁶⁵ CAW-2 (Owens) at 29.

⁶⁶ CAW-2 (Owens) at 27.

⁶⁷ CAW-2 (Owens) at 27.

⁶⁸ CAW-2 (Owens) at 14-15. One of the first applicable Commission decisions following the implementation of §§ 2718 – 2720 was D. 01-09-057, authorizing Cal-Am to acquire the water utility assets and public utility operations of Citizens Utilities Company of California. In this decision, the Commission explains the conundrum of how an increased rate base, with a likely increase in rates to follow, is beneficial to ratepayers of the acquired company “.....that if it were to include the full acquisition premium directly in rate base at the time of transfer under Section 2720(a), the revenue requirement for the former Citizens districts would be driven up and rates would follow in the short term. Economies of scale would begin to develop almost immediately, however, and after the early years the synergies savings from consolidation would overcome the effects of including the acquisition adjustment in rate base. Rates could then begin to drop to below what they would have been for the stand-alone operation.”

beyond the usual annual attrition adjustments, until Cal-Am has litigated its next 2024 GRC. While we note the rate impacts attributed by this Proposed Acquisition, the Commission is interested in reviewing the broader rate impacts for Warring customers in the GRC venue.

While the rate impacts of this Proposed Acquisition cannot be completely eliminated, those ratepayer impacts are one of several components comprising the public interest driven by an increase in rate base determined to be fair and reasonable. In view of the compelling evidence of public interest benefits, identified here, that will result from the Proposed Acquisition, we find that on balance the Proposed Acquisition promotes the legislatively declared post-transaction public interest objectives and meets the “ratepayer indifference standard.”

5.4. Operational Consolidation, Ratemaking Consolidation and Allocation of New Rate Base

The Joint Applicants proposed immediate operational consolidation of Warring and deferred ratemaking consolidation of Warring until the next Cal-Am GRC with implementation of new rates anticipated in 2024. Since most of the synergies and cost savings of the Proposed Acquisition occur with operational consolidation, this decision approves immediate operational consolidation. This decision also approves ratemaking consolidation after Cal-Am’s next GRC, consistent with Pub. Util. Code § 451 *et seq.*

Cal-Am’s proposed allocation of new rate base and the associated new \$322,100 in revenue is designed to minimize the rate increase by collecting it equally over the largest number of customers possible (all Cal-Am customers statewide).⁶⁹ The Joint Applicants’ proposed allocation, and calculation of rate

⁶⁹ Application at 17; CAW-2 (Owens) at 9-10.

and bill impacts, is illustrative, as it necessarily depended upon a number of assumptions, as follows:

- Commission approval of new rates proposed by Cal-Am in its 2019 GRC A.19-07-004,
- Current total bills and surcharges in effect at the time the application was filed,
- timing of integration,
- synergies from operational consolidation materialize in the amounts estimated, and
- synergies from operational consolidation are incorporated in the first year after the acquisition is completed.⁷⁰

Most of the assumptions made to estimate the new revenue requirement, and propose allocation of new rate base, have changed due to the passage of time, or, as indicated by the Cal-Am witness, were made for calculation purposes only (synergies incorporated in the first year) and did not reflect reality. Cal-Am already planned to defer ratemaking consolidation until its next GRC, so it is unnecessary to set an allocation in this decision.

There is some guidance in § 854(e), to avoid adverse consequences of the transaction if an alternative to capturing savings can be found. Moving the allocation decision closer to the time when new rates will take effect, and better estimates can be made, enhances the prospect of understanding rate impacts and apportioning impacts most fairly.

In the absence of a viable alternative analysis now, this decision does not approve Cal-Am's proposed allocation of rate base. Instead, we defer the allocation to the next GRC, where the estimates of revenue requirement, rate and bill impacts will be refreshed. At that time, Cal-Am and intervenors will have an

⁷⁰ CAW-2 (Owens) at 12-14.

opportunity to fully analyze the correct basis for setting rates in all of Cal-Am's districts including the new Southern District which will include the former Warring customers.

The Warring customers continue to be served at present rates, subject to the same interim attrition rate adjustments that would have been available to Warring under the current ratesetting regime, until there is a decision in the next GRC where Cal-Am will have Warring consolidated into its overall operations.

5.5. Notice to Cal-Am Customers

The scope of this proceeding includes whether notice of the proposed transaction was properly provided to those impacted by the proceeding, including Warring customers and all Cal-Am customers statewide. The Commission applies the notice requirements of D.99-10-064 to proposed water acquisitions such as the instant application. Here we also apply the notice requirements of D.99-10-064 as such guidance is expressly applicable to applications governed by the Consolidation Act.⁷¹

Cal-Am inserted into customer bills a notice of the application, dated April 28, 2021. Warring directly mailed its customers a notice of the application dated May 5, 2021. The notices to customers sent to Cal-Am and Warring customers describe the estimate rate impact to typical residential customers in both dollar and percentage terms, as required. Notices informed affected customers of Commission process of considering the application, names and contact information for additional information, and how to directly comment on the application. Subsequent to the mailing of the notices, nine individuals

⁷¹ Section 4.03 of the settlement agreement approved by D.99-10-064 contains guidance on notice to affected customers.

commented on the Commission's docket card, all opposed to the rate increases associated with the transaction.

We find that Joint Applicants provided adequate notice of the Proposed Acquisition to affected customers in accordance with D.99-10-064.

5.6. New and Modified Memorandum Accounts

The Joint Applicants request the Commission establish for Cal-Am two new memorandum accounts: (i) The Warring Acquisition Contingency Memorandum Account⁷² (Contingency Account), which would track alleged lost revenue from all affected entities until the acquisition could be integrated for ratemaking purposes in the 2024 GRC; and (ii) The Warring Transaction Cost Memorandum Account (Transaction Account) which would track any potential costs necessary to complete the transaction, such as legal, engineering, surveying, appraisal, noticing, and other professional activities not otherwise included in the application.

As discussed below, we deny the request to create the Contingency Account and approve the Transaction Account subject to certain conditions, as discussed below; and we approve the inclusion of Warring in Cal-Am's existing Memorandum Account for Environmental Improvements and Compliance.

⁷² A memorandum account is a regulatory tool that, when authorized, allows a utility to record off the balance sheet any costs which are defined but unknown in terms of amount or justification. These defined costs are not yet authorized as recoverable in rates. In a subsequent proceeding the utility must (1) justify why the costs should be recoverable from ratepayers and then it must (2) justify the costs were reasonably incurred (*e.g.*, costs were as low as possible, etc.) Thus, a memorandum account is a promise to consider recovery, not a promise of recovery in subsequent rates. The creation of a memorandum account avoids the legal prohibition on retroactive ratemaking.

5.6.1. The Warring Acquisition Contingency Memorandum Account

Cal-Am requests authority to create a Contingency Account to track, until the implementation of new rates associated with the new rate base approved in this decision, the difference between revenue collected from customers at current rates, and revenue that would have been collected had ratemaking consolidation occurred immediately instead of after Cal-Am's next GRC.⁷³ The Joint Applicants' estimate of revenues that may be lost during the years before consolidation occurs should be the same as the revenues calculated for illustrative purposes if the acquisition were to close immediately, which is \$322,100, annually.

The Joint Applicants' argument for the Contingency Account is identical to those made for a Contingency Account in its A.20-04-003 to acquire East Pasadena Water Company.⁷⁴ While the Commission is not rigidly bound to precedent, this most recent prior Commission decision approving Cal-Am's acquisition found that Cal-Am had no need for a Contingency Account and denied such request.⁷⁵ The same reasoning in D.21-08-002 applies here. In that decision, the Commission reasoned that, as an experienced and:

"...competent entity Cal-Am should have recognized that the price it would pay would include the attendant risks and opportunities offered by Warring's current and near-term operations and revenue stream as well as the open-ended opportunity for a future revenue stream as a part of Cal-Am's overall operations."⁷⁶

⁷³ Application at 18.

⁷⁴ CAW-2 (Owens) at 15-18.

⁷⁵ D.21-08-002, Finding of Fact (FoF) 20, OP 8.

⁷⁶ D.21-08-002 at 34.

Here however, the length of time between the close of this transaction and Cal-Am's application for new rates is likely to be much shorter than anticipated, further reducing the need to reconcile any revenue differences prior to the implementation of new rates.

We therefore find, as we recently did in D.21-08-002, that there is no "contingency" or other circumstances that warrant the creation of the proposed Contingency Account and deny this request.

5.6.2. The Warring Transaction Cost Memorandum Account

The Transaction Account would track the costs of activities necessary to complete the transaction, such as legal, engineering, surveying, appraisal, noticing, and other professional activities. In support of their requests for both memorandum accounts, the Joint Applicants argued the requests (for both the Contingency Account and Transaction Account) meet the Commission's four criteria for creating memorandum accounts and are consistent with recent Commission decisions approving Cal-Am's other acquisitions.

One criterion for approval of a memorandum account is that the cost be of a substantial nature, yet Cal-Am provides no amount or estimate of transaction costs in its testimony, rather stating generally, "Transaction costs are inherent in the acquisition of smaller water systems and the acquiring company should receive due consideration of recovery of these costs."⁷⁷ Cal-Am is a sophisticated party that has purchased other water systems and is more than capable of weighing its risks and rewards by entering into the agreement to buy Warring's operations, and it has had every opportunity to include in this application all foreseeable costs in addition to the purchase price.

⁷⁷ CAW-2 (Owens) at 18.

Nevertheless, this decision follows the rationale of the most recent Commission approval of Cal-Am's acquisition East Pasadena, and we grant the request to authorize a Transaction Account. However, this authorization is limited to tracking for potential recovery of costs incurred after the effective date of this decision, subject to review by the Commission in a subsequent proceeding.⁷⁸ We remind all parties that this is a Memorandum Account. As such there is no presumption that the costs will be found necessary or reasonable and, instead, they may not be recoverable. Merely spending the money does not justify future recovery in rates. Cal-Am bears the full burden of proof for both the necessity of these costs and their reasonableness. "Necessity" means that these costs benefit the customers by improving or maintaining the system in a reasonable manner to provide safe and reliable water service.

**5.6.3. Inclusion of Warring in the Existing
Memorandum Account for Environmental
Improvements and Compliance Issues for
Acquisitions**

Cal-Am's request to expand the currently authorized memorandum account entitled "The Memorandum Account for Environmental Improvements and Compliance issues for Acquisitions" is granted. This is consistent with decisions in prior acquisitions and is in the public interest. As with all memorandum accounts, it is subject to review before any recovery is included in rates.

6. Interim Rate Relief Until the Next GRC

Until Cal-Am has its 2024 GRC, Cal-Am requested permission to file for the annual cost-of-living rate increases the Commission would have permitted for Warring had the acquisition not occurred. We find that the impact of the

⁷⁸ D.21-08-002, at 35-36, FoF 21.

annual cost-of-living rate increases on Warring customers is reasonable because these filings would have occurred in the absence of the acquisition. Cal-Am is granted the interim rate relief as requested.

7. Certificate of Public Convenience and Necessity

Upon completion of the acquisition, Warring will cease to operate and Cal-Am will replace it as the service provider for the current customers of Warring. Consequently, we must simultaneously cancel Warring's CPCN and modify Cal-Am's CPCN to include the new service territory and customers. Upon completion of the transaction both Warring and Cal-Am shall file Tier 1 compliance advice letters to implement these respective changes.

8. The California Environmental Quality Act

Pursuant to Public Resources Code § 21065 *et seq.* (the California Environmental Quality Act (CEQA)) and pursuant to Rule 2.4 of the Commission's Rules of Practice and Procedure, the Commission must consider the environmental consequences of projects that are subject to our discretionary approval.

The CEQA Guidelines state that a proposed "activity [that] will not result in a direct or reasonably foreseeable indirect physical change in the environment" is exempt from CEQA.⁷⁹ Similarly, where "it can be seen with certainty that there is no possibility that the [proposed] activity in question may have a significant effect on the environment, the activity is not subject to CEQA."⁸⁰

As stated by the Joint Applicants, "once sold and transferred, there will be no change in the operation of the Warring Assets. They will be used and

⁷⁹ CEQA Guideline § 15060(c)(2).

⁸⁰ CEQA Guideline § 15061(b)(3).

operated in the same manner and for the same purposes for which they are currently being used – to provide water service.”⁸¹

We therefore find that the Proposed Acquisition is not subject to CEQA review, as we find there is no possibility that the Proposed Acquisition may have a significant effect on the environment.

9. Safety Considerations

The Proposed Acquisition does not appear to cause any change in any aspects of safety as to the operation of the Warring service area. To the contrary, Joint Applicants assert Cal-Am’s commitment to safety is reflected in

- Its work to eliminate OSHA [Occupational Safety and Health Administration] violations;
- Implementation of safety programs designed to protect the workforce and customers;
- Assessments of system vulnerabilities to wildfires, Public Safety Power Shutoffs, and terrorist acts; and
- Formulating response plans.⁸²

We therefore find that safety is not negatively impacted by this Proposed Acquisition, and that this Proposed Acquisition complies with § 451, which requires, in part, that utilities are operated to promote the safety of the public.

10. Comments on Proposed Decision

The proposed decision of Administrative Law Judge Watts-Zagha in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and comments were allowed under Rule 14.3 of the Commission’s Rules of Practice and Procedure. Comments were filed on _____, and reply comments were filed on _____ by _____.

⁸¹ Application at 23.

⁸² Application at 21-22.

11. Assignment of Proceeding

John Reynolds is the assigned Commissioner and Camille Watts-Zagha is the assigned ALJ in this proceeding. Pursuant to § 1701.3(b) and Rule 13.2(b), ALJ Watts-Zagha was designated as the Presiding Officer.

Findings of Fact

1. Cal-Am is a Class A public water utility subject to the jurisdiction of this Commission. Cal-Am is a California corporation and it is a subsidiary of American Water Works Company, the largest publicly traded water utility in the United States.

2. Cal-Am has a CPCN to operate as a regulated Class A public water utility company and serves approximately 680,000 people in 50 communities in California.

3. Warring is a Class D public water utility subject to the jurisdiction of this Commission.

4. Warring has a CPCN to operate as a regulated Class D public water utility serving approximately 518 customers in and near Piru, Ventura County, California.

5. Cal-Am and Warring adequately notified their customers of the proposed acquisition of Warring's utility assets.

6. Commission Resolution W-4796 has previously established Warring's rate base of \$745,867 with a revenue requirement of \$500,800.

7. Cal-Am forecasts Warring's rate base in 2021 to be \$1.384 million and Warring's revenue requirement in 2021 to be \$644,100.

8. Cal-Am's request in its 2019 GRC proceeding A.19-07-004 to consolidate, for ratemaking purposes, its Los Angeles County District with Ventura County

District and San Diego County District in a new Southern Division was approved in D.21-11-018.

9. Cal-Am is scheduled to file its next GRC application on July 1, 2022, for test year 2024.

10. Warring's owners voluntarily entered into an agreement to sell the utility's assets to Cal-Am in an arm's-length negotiated contract at a mutually agreeable price of \$4.6 million, with minor adjustments at closing the transaction, for all of Warring's water system related assets used to operate as a Class D water public utility.

11. The proposed purchase price is \$4.6 million, plus or minus any adjustment amounts within the purchase agreement.

12. The Consolidation Act provides that an acquisition premium may be included in the acquiring water company's rate base. This acquisition premium is the difference between the book value of the assets prior to acquisition, and the fair market value of the assets at the time they are purchased.

13. As long as the transaction is found to be in the public interest, the Consolidation Act permits inclusion of the acquisition premium in the acquiring company's rate base.

14. Warring can be operationally included in Cal-Am's current Ventura County District.

15. Warring's rates for its current customers, including any allowable rate increase, remain in effect until Cal-Am's test year 2024 GRC decision.

16. The Proposed Acquisition will result in efficiencies and economies of scale which would benefit the existing Warring and Cal-Am ratepayers, including benefits from operationally consolidating Warring into the Cal-Am Ventura

County District and from consolidating, for ratemaking purposes, Warring into the Southern Division.

17. The proposed purchase price was supported by the Joint Applicants' appraisal, which was based on the replacement cost new less depreciation method. The appraisal valued the Warring system assets at \$5.3 million, consisting of tangible property assets valued at \$4.4 million and real estate valued at \$973,000.

18. As a large Class A water utility, Cal-Am is in a superior position to achieve economies of scale, resources, and has knowledge to better service the water needs of the Warring service area compared to Warring's current operations.

19. Cal-Am has no need for a new Warring Acquisition Contingency Memorandum Account.

20. Cal-Am needs a new Warring Transaction Cost Memorandum Account for potential recovery of costs incurred after the effective date of this decision.

21. Cal-Am needs to include Warring in an existing Memorandum Account for Environmental Improvement and Compliance Issues for Acquisitions.

22. The cost allocation and rate design impacts of the acquisition can be deferred to the 2024 GRC.

23. The Proposed Acquisition will enhance the health and safety of Warring customers.

24. The Proposed Acquisition will have no reasonably foreseeable impact on the environment.

25. The Proposed Acquisition is not subject to CEQA as it can be seen with some certainty that there is no possibility that the transaction in question may have a significant effect on the environment.

26. The Proposed Acquisition is exempt from CEQA review, pursuant to CEQA Guideline § 15061(b)(3).

Conclusions of Law

1. The Joint Applicants motion dated March 26, 2021 to admit exhibits into the evidentiary record should be granted.

2. The Commission should authorize Warring to sell, and Cal-Am to purchase, all of Warring's assets listed the Asset Purchase Agreement, entered into on August 19, 2019, including Warring's entire water system and all of its assets.

3. The total final purchase price of \$4.6 million, plus or minus any adjustment amounts within the Asset Purchase Agreement, represents the fair market value as defined by Pub. Util. Code § 2720.

4. The rate impacts associated with an estimated \$322,100 increase in revenue requirement are reasonable in view of the compelling evidence of public interest benefits that will result from the proposed transaction.

5. The Commission should authorize post-transaction rate base equal to the total final purchase price.

6. Approving Cal-Am's proposed purchase of the water utility assets of Warring is in the public interest and consistent with §§ 851 *et seq.* and §§ 2718 *et seq.*

7. The Application and the proposed acquisition promote the legislative and public interest goals of Public Water System Investment and Consolidation Act, §§ 2718 *et seq.*

8. It is reasonable to direct the parties to address the long-term ratemaking options and consequences of the intangible assets in the 2024 GRC.

9. Consideration of Cal-Am's proposal to allocate the rate base between the newly consolidated Southern Division and its Corporate Office, which would impact all Cal-Am's ratepayers statewide, should be deferred to the next 2024 GRC.

10. Cal-Am's proposed immediate consolidation of the Warring service area with Cal-Am's Ventura County District service area, for operational purposes, should be authorized.

11. Cal-Am's request to consolidate Warring into its new consolidated Southern Division for ratemaking purposes in Cal-Am's next GRC, effective January 1, 2024, is reasonable, and should be granted.

12. The ratemaking allocation of the rate base addition should be deferred to the 2024 GRC.

13. Until Cal-Am files its next GRC, the rates in the Warring service area should remain in effect subject to existing authority to file for rate increases using the Commission's advice letter process.

14. Cal-Am's request for authorization to establish a Warring Transaction Memorandum Account to record all of its future transaction costs consistent with this Decision should be granted.

15. Cal-Am's request for authorization to establish a Warring Acquisition Contingency Memorandum Account should be denied.

16. Cal-Am should be authorized to add Warring to its existing Memorandum Account for Environmental Improvement and Compliance Issues for Acquisitions.

17. The transaction complies with and is consistent with § 451, which requires, in part, that utilities are operated to promote the safety of the public.

18. This proceeding should be closed.

O R D E R**IT IS ORDERED** that:

1. Warring Water Service, Inc. (Warring) is authorized to sell, and California-American Water Company is authorized to purchase, all of Warring's assets listed in the Asset Purchase Agreement, entered into on April 16, 2019, including Warring's entire water system, water rights and all of its assets.

2. California-American Water Company's (Cal-Am's) Certificate of Public Convenience and Necessity is modified to incorporate the Warring Water Service, Inc. service area into Cal-Am's Ventura County District or Southern Division.

3. California-American Water Company (Cal-Am) is authorized to include the \$4,600,000 purchase price, plus or minus any adjustment amounts within the purchase agreement, of Warring Water Service, Inc. in Cal-Am's rate base in a subsequent 2024 general rate case proceeding. Cal-Am shall address the long-term ratemaking treatment of the acquired assets in that proceeding.

4. California-American Water Company, in its next 2024 general rate case, shall consolidate Warring Water Service, Inc. in its Southern Division tariffs for ratemaking purposes.

5. California-American Water Company's (Cal-Am's) proposed immediate consolidation of the Warring Water Company service area with Cal-Am's Ventura County District service area, for operational purposes, is authorized.

6. Existing rates for customers of the Warring Water Service, Inc. shall remain in effect until subsequently modified by this Commission.

7. California-American Water Company shall file within 10 days of this decision a Tier 1 Advice Letter to establish a Warring Transaction Cost Memorandum Account and to include Warring in its existing Memorandum

Account for Environmental Improvement and Compliance Issues for Acquisitions.

8. California-American Water Company's request to create a new Warring Acquisition Contingency Memorandum Account is denied.

9. Until California-American Water Company files its 2024 general rate case proceeding, the rates in the Warring Water Service, Inc. service area shall remain in effect subject to existing authority to file for rate increases using the Commission's advice letter process.

10. California-American Water Company's request for authorization to establish a Warring Transaction Memorandum Account to record all of its future transaction costs consistent with this Decision is granted.

11. Within 10 days of the completion of the sale by the Warring Water Service, Inc. (Warring) to California-American Water Company (Cal-Am) of all of the assets included in the Asset Purchase Agreement, Cal-Am and Warring shall notify the Commission's Water Division that the sale has been completed.

12. The joint motion filed by California-American Water Company and Warring Water Service, Inc. on March 26, 2021, to admit exhibits into the evidentiary record is granted, and those exhibits are identified and received into evidence as listed below.

Exhibit Number	Sponsor/Witness	Description
CAW-1	Cal-Am/Hofer	Direct Testimony of Garry M. Hofer, Public Version, dated April 27, 2020
CAW-1C	Cal-Am/Hofer	Direct Testimony of Garry M. Hofer, Confidential Version, dated April 27, 2020
CAW-2	Cal-Am/Owens	Direct Testimony of Stephen Wesley Owens, dated April 27, 2020

CAW-3	Cal-Am/Wademan	Direct Testimony of Michael Wademan, dated April 27, 2020
WWS-1	WWS/Brommenschenkel	Direct Testimony of Frank Brommenschenkel dated April 27, 2020
WWS-2	WWS/Pace	Direct Testimony of Glen Pace, dated April 27, 2020
JA-1	JA/Zanni	Direct Testimony of Kevin M. Zanni, dated April 27, 2020

13. Application 20-04-017 is closed.

This order is effective today.

Dated _____, at Sacramento, California.